

**ALABAMA PREPAID AFFORDABLE
COLLEGE TUITION PROGRAM**

SEPTEMBER 30, 2007

FINANCIAL STATEMENTS

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM
MONTGOMERY, ALABAMA

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ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM
MONTGOMERY, ALABAMA

MANAGEMENT'S DISCUSSION & ANALYSIS
SEPTEMBER 30, 2007

The following is designed to provide an understanding of various factors related to the Alabama Prepaid Affordable College Tuition (PACT) Program's operations and financial condition. This information should be read in conjunction with the financial statements and related notes. The purpose of this information is to focus on significant changes in the financial condition during the fiscal year ended September 30, 2007, and highlight events that occurred during the year.

The PACT Program is classified as a fiduciary fund in the State of Alabama Comprehensive Annual Financial Report (CAFR).

Assets

The assets of the PACT Program include cash, receivables, investments, and other assets. Assets were \$898,548,289 and \$772,760,941 as of September 30, 2007 and 2006, respectively. The largest increase in assets of \$71.2 million is a result of the introduction of securities lending activities during this fiscal year. The remaining increase is due to the favorable market value of investments at September 30, 2007.

The composition of the Program's investment securities portfolio reflects the PACT Board's investment strategy of strategic asset allocation for an efficient, well diversified and manageable portfolio for the long term, while maintaining an appropriate level of liquidity to meet tuition benefit obligations. The Board reviews asset allocation annually. The current target asset allocation of the fund is 51% domestic equity, 21% developed foreign country equity and 28% fixed income securities. Asset rebalancing of the investment portfolios may occur as markets fluctuate. To diversify Program assets so as to minimize the risk associated with the dependence on the success of one enterprise, the Board has selected ten managers to invest plan assets. At fiscal year-end, the Program had limited exposure of approximately 2.2% of subprime mortgage investment rated AAA. No downgrades or defaults have been experienced by the portfolio, and none are expected.

The Board has also contracted with an investment consultant to evaluate, monitor, and report on the investment portfolio and investment manager returns, to provide risk/return assumptions on investments, to recommend diversification, to perform asset liability studies, and to monitor compliance with the adopted investment policy. The Investment Policy and Manager Guidelines are reviewed, revised, and approved by the Board annually.

The following table represents the Program's investment portfolio, asset allocation, and corresponding annual rates of return as of September 30, 2007. Cash and cash equivalents are excluded.

ASSET CATEGORY	MARKET VALUE	PERCENT	ANNUAL RETURN (NET OF FEES)
Fixed income	\$ 200,268,867	25.52%	5.53%
Domestic equity	405,215,434	51.64%	15.36%
International equity	179,198,821	22.84%	26.71%

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The following table represents the Program's investment portfolio, asset allocation and corresponding annual rates of return as of September 30, 2006. Cash and cash equivalents are excluded.

ASSET CATEGORY	MARKET VALUE	PERCENT	ANNUAL RETURN (NET OF FEES)
Fixed income	\$ 213,131,123	29.32%	4.74%
Domestic equity	355,499,067	48.90%	10.43%
International equity	158,382,948	21.78%	15.11%

Liabilities

Liabilities of the PACT Program consist of payables and accruals. Liabilities were \$134,689,600 and \$81,165,753 (as restated) at September 30, 2007 and 2006, respectively. The increase in liabilities was primarily due to \$71.2 million in securities lending collateral. Warrants and accounts payable include Fall semester tuition benefits payable of \$25.7 million and \$22.7 million (restated) at September 30, 2007 and 2006, respectively. As described in Note 6, PACT has adopted the practice of recording the Fall semester tuition benefits as a payable. Previously, this payable was captured in the actuarial present value of future benefit payments. The 2006 financials have been restated to reflect this change.

Other liabilities consist of forward settling TBA mortgage-backed securities of \$35.3 million and \$55.8 million at September 30, 2007 and 2006, respectively. These securities and amounts are within the acceptable guidelines of the Investment Policy.

Additions

Additions totaled \$135,401,839 and \$95,583,512 for fiscal years ended September 30, 2007 and 2006, respectively. The largest addition for fiscal year 2007 was the net increase in fair value of investments which was \$83,073,338 compared to \$47,271,312 for the fiscal year ended September 30, 2006. Investment income increased 17.95% over 2006.

A securities lending program was initiated in May 2007, resulting in net income to PACT of \$53,432 for the fiscal year. The program, administered by the program's custodian Bank of New York Mellon (BNY Mellon), was authorized by the Board. BNY Mellon is an industry leader in securities lending with a comprehensive indemnification and strong credit/risk control culture. U.S. Government securities, corporate securities, and U.S. equities are lendable. At year-end, PACT securities lending activity was comprised of \$7.8 million domestic fixed securities, and \$60.9 million domestic equity.

Contract payments remained fairly stable over last year, increasing 3%, due to the slight increase in number of contracts sold. Other income, consisting primarily of administrative fees for processing of contract payments, increased 14.6%. There were no fee increases; however, generally more fees were generated and collected.

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Deductions

Deductions totaled \$63,138,338 and \$56,019,736 for fiscal years ending September 30, 2007 and 2006, respectively. Deductions include salaries, professional services, contract cancellation refunds, and benefits paid to colleges and universities.

The largest deduction from the Program is the amount of monies paid to the colleges and universities for tuition and qualified fees. It is expected this amount will increase every year as the Program ages with more contracts eligible for benefit payments and college tuition increases. For fiscal year ending 2007 the Program paid \$54.9 million to over 400 colleges and universities across the nation for approximately 12,400 beneficiaries, as compared to \$48.6 million paid in fiscal year ending 2006.

Professional service expenses increased approximately 17% over 2006. The increase was largely due to the increased fees paid to investment managers. These fees are based on market value of assets and the market value increased throughout the year. Additionally, a marketing firm was hired and approximately \$90 thousand was paid to the firm to facilitate the development of a one-year marketing plan, redesign the website, compile and print the enrollment kit, and compose and place television advertising.

Summary

The primary objective of PACT is to accumulate sufficient assets to pay tuition and qualified fee benefits to higher education institutions on behalf of beneficiaries when due. For the fiscal year ending 2007, the PACT Program had net assets of \$763,858,689. When adding the actuarial present value of future contract payments of \$53.3 million to net assets and dividing by the actuarial present value of future tuition benefit payments of \$836.9 million, the result is an actuarial funded status of 97.6% of its liabilities. This is an increase over the 2006 actuarial funded status of 92.5%. The increase in the actuarial funded status results from better than assumed investment performance, lower than assumed tuition increases, and a favorable increase in the fair value of assets. Actuarial assumptions are reviewed and approved by the Board annually to reflect expected results believed to be realistic based on historical information, economic data and expert guidance. The 2007 Actuarial Report is available on the Treasurer's website. The report should be read in its entirety so that the projections can be properly interpreted.

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM
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STATEMENT OF FIDUCIARY NET ASSETS
SEPTEMBER 30, 2007

ASSETS:

Cash and cash equivalents	\$ 38,535,954
Interest and dividends receivable	2,382,986
Foreign taxes receivable	375,799
Other receivables	1,311,259
Investments	784,683,122
Invested securities lending collateral	71,259,169
Total assets	<u>898,548,289</u>

LIABILITIES:

Amounts due to State Treasury	36,129
Warrants and accounts payable	28,022,683
Accrued liabilities	75,334
Other liabilities	35,296,285
Securities lending collateral	71,259,169
Total liabilities	<u>134,689,600</u>

NET ASSETS:

Held in trust for tuition payments and other purposes	<u>\$ 763,858,689</u>
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The accompanying notes are an integral part of these financial statements.

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

STATEMENT OF CHANGE IN FIDUCIARY NET ASSETS FOR THE YEAR ENDED SEPTEMBER 30, 2007

ADDITIONS:

Contract payments	<u>\$ 28,865,379</u>
Investment income:	
From investing activities:	
Interest and dividend income	22,545,340
Net increase in fair value of investments	<u>83,073,338</u>
Net investment income from investing activities	<u>105,618,678</u>
From securities lending:	
Securities lending income	1,167,482
Less: securities lending expenses	
Borrower rebates	1,091,314
Management fees	<u>22,736</u>
Total securities lending expenses	<u>1,114,050</u>
Net income from securities lending activities	<u>53,432</u>
Total investment income	<u>105,672,110</u>
Other income	<u>864,350</u>
Total additions	<u>135,401,839</u>

DEDUCTIONS:

Benefits	54,885,211
Salaries and other administrative expenses	345,389
Professional services	3,926,219
Cancellation refunds	<u>3,981,519</u>
Total deductions	<u>63,138,338</u>

CHANGE IN NET ASSETS	<u>72,263,501</u>
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NET ASSETS AT BEGINNING OF YEAR AS ORIGINALLY STATED	714,255,990
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PRIOR PERIOD ADJUSTMENT	<u>(22,660,802)</u>
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NET ASSETS AT BEGINNING OF YEAR (AS RESTATED)	691,595,188
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NET ASSETS AT END OF YEAR	<u>\$ 763,858,689</u>
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The accompanying notes are an integral part of these financial statements.

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Description of Alabama Prepaid Affordable College Tuition Program (the PACT Program) - The PACT Program is a part of the Wallace-Folsom College Savings Investment Plan. The PACT Program includes the PACT Trust Fund and the PACT Administrative Fund. These financial statements do not include any other programs of the Wallace-Folsom College Savings Investment Plan.

The PACT Program operates under the provisions of the Code of Alabama 1975, Section 16-33C-1 through 9, as amended. The PACT Program is administratively located within the Alabama State Treasurer's office. The PACT Program's property, income, and operations have been statutorily exempted from all taxation by the State and its political subdivisions. The act and the contracts do not specify that the State, the Treasurer, or the Board is liable if the PACT Program becomes actuarially unsound.

The PACT Program is governed by a ten-member Board of Trustees consisting of the Treasurer of the State of Alabama, the Lieutenant Governor or designee, the executive director of the Alabama Commission on Higher Education or designee, the chancellor of the Alabama Department of Postsecondary Education or designee, each of whom shall serve ex officio; a representative of the Council of College and University Presidents; one person appointed by the Treasurer; one person appointed by the Speaker of the House of Representatives; one person appointed by the Lieutenant Governor; and two persons appointed by the Governor.

The PACT Program enters into a contract with a purchaser which provides that, in return for a specified actuarially determined payment, the PACT Program will provide a child's undergraduate tuition and qualified fees (up to 128 semester hours) at any Alabama public university or community college. For beneficiaries that choose to attend private or out-of-state institutions, the PACT Program will provide tuition payments at the current weighted average cost of tuition at Alabama public four-year institutions. The purchase amount is based on several factors, including tuition costs, the beneficiary's age and grade in school, anticipated investment earnings, and anticipated tuition rate increases.

Reporting entity - The PACT Program is a part of the State of Alabama's reporting entity and is reported as a fiduciary fund in the State of Alabama Comprehensive Annual Financial Report (CAFR). The notes accompanying these financial statements relate directly to the PACT Program.

Measurement focus and basis of accounting - The financial statements contained in this report are prepared using the economic resources measurement focus and the accrual basis of accounting.

Cash and cash equivalents - The PACT Program considers all highly liquid investments with a maturity of twelve months or less at the time of issue to be cash equivalents. Cash and cash equivalents consist of bank deposits, amounts invested in repurchase agreements, money market mutual funds and securities rated A-1 by Moody's, P1 by Standard & Poor's or better by a recognized credit rating service.

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NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

Investments - All plan investments are reported at fair value in the statement of fiduciary net assets, with all investment income, including changes in fair value, reported as additions in the statement of change in fiduciary net assets. Fair values for investment securities are based on quoted market prices, where available. Otherwise, fair values are based on quoted market prices of comparable instruments.

NOTE 2 - CASH AND CASH EQUIVALENTS:

Cash and cash equivalents at September 30, 2007 consist of the following:

<u>ACCOUNT TYPE</u>	<u>FAIR VALUE</u>
Interest earning deposits	\$ 882,496
Money market mutual funds	32,268,458
Repurchase agreements	<u>5,385,000</u>
	<u>\$ 38,535,954</u>

NOTE 3 - DEPOSITS AND INVESTMENTS:

As of September 30, 2007, the Program had ten money managers to invest plan assets. The Program also has an investment consultant who assists the Board of Trustees in monitoring compliance with the Program's investment policy and monitoring performance of the money managers.

Deposits and investments are subject to certain types of risk including interest rate risk, custodial credit risk, and foreign currency risk. The following describes those risks.

Deposits - Custodial credit risk - The Program maintains its cash in bank deposit accounts, which at times may exceed federally insured limits. The Program has not experienced any losses in such accounts. The Program believes it is not exposed to any significant credit risk.

Investments - Interest rate risk - The fair value of fixed-maturity investments fluctuate in response to changes in market interest rates. Increases in prevailing interest rates generally translate into decreases in fair value of those instruments. The fair value of interest sensitive instruments may also be affected by the creditworthiness of the issuer, prepayment options, relative values of alternative investments, and other general market conditions. Certain fixed maturity investments have call provisions that could result in shorter maturity periods.

Custodial credit risk - For an investment, custodial credit risk is the risk that an entity will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party if the counterparty fails. The PACT Program's custodian holds all investments of the PACT Program in the PACT Program's name, with the exception of repurchase agreements. The securities underlying repurchase agreements are held in trust for the PACT Program in the name of the trustee, not in the name of the PACT Program.

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

NOTE 3 - DEPOSITS AND INVESTMENTS: (continued)

Credit quality - Nationally recognized statistical rating organizations provide ratings of debt securities quality based on a variety of factors, such as the financial condition of the issuers, which provide investors with some idea of the issuer's ability to meet its obligations. Fixed-maturity investments may consist of domestic securities with an initial Moody's, Standard & Poor's, or Fitch's quality rating of Baa3, BBB-, or BBB-, respectively, at a minimum. The PACT Program's investment policy states that debt securities that are downgraded below the minimum level defined above should be sold within a six-month period of such downgrade. However, certain investment managers of the PACT Program are permitted to invest in "below investment grade" quality bonds, non-U.S. dollar denominated bonds, and emerging market debt, provided that the amount invested in these securities is limited to 30% of the market value of the investment manager's portfolio. At September 30, 2007, 95.3% of the PACT Program's investments in fixed investment securities were rated as investment grade. Cash and cash equivalents are required to be invested in money market mutual funds backed by securities of the U.S. Government and federal agencies or other securities rated A-1 by Moody's, P-1 by Standard & Poor's or better by a recognized rating service.

Foreign currency risk - For an investment, foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. In order for an international equity security to be eligible for purchases by the PACT Program, the issuing company must have an available operating history of at least three years, and have a market capitalization of at least \$100 million at the time of purchase.

Concentration of credit risk - The investment policies limit the aggregate amount that can be invested in each class of investments and provides further limitations on investments by individual money managers. The policy limits are as follows:

- Domestic fixed income and cash
 - Limited to 28% of the market value of the aggregate portfolio, plus or minus 5%. With the exception of those situations involving reorganization of fund assets, debt investments should only be made in issues with an outstanding value of at least \$50 million, valued at par, at the time of purchase.
 - On an individual money manager basis, no more than 5% of the total market value of all debt investments should be invested in the debt obligations of any one issuer, with the exception of securities issued and collateralized by the United States Government, or its agencies, or collateralized by the U.S. Government, which may be held without limitation. Holdings of any individual issue must be 5% or less of the outstanding value of the total issue.
- Domestic Equity
 - Large/mid cap stocks - Limited to 42% of the market value of the aggregate portfolio, plus or minus 5%.
 - Small cap stocks - Limited to 9% of the market value of the aggregate portfolio, plus or minus 3%.

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NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

NOTE 3 - DEPOSITS AND INVESTMENTS: (continued)

- The PACT Program's investment policy states that equity holdings will be restricted to readily marketable securities of corporations that are actively traded on major exchanges including the NASDAQ in the U.S. Equity holdings may include American Depositary Receipts traded on U.S. exchanges. Preferred and convertible preferred stocks may be held. Publicly traded Real Estate Investment Trust (REITs) shares may be held and are considered part of the allocation to stocks. The policy is to invest in equity securities of issuers with an available operating history of at least three years, and a market capitalization of at least \$50 million at the time of purchase.
- On an individual money manager basis, no more than 5% of the total stock portfolio may be invested in the common stock of any one corporation at the time of purchase, and no more than 7% in any one corporation at fair market value. No more than 5% of the outstanding shares of any one company may be held. No more than the lesser of three times the sector weight in the index and 40% valued at market may be held in any one economic sector.
- International Equity
 - Limited to 21% of the market value of the aggregate portfolio, plus or minus 3%. Equity holdings may include American Depositary Receipts and Global Depositary Receipts traded on U.S. exchanges or major exchanges in countries outside the United States. Convertible and non-convertible preferred stocks may be held. The policy is to invest in equity securities of issuers with an available operating history of at least three years, and a market capitalization of at least \$100 million at the time of purchase.
 - On an individual money manager basis, no more than 5% of the total stock portfolio may be invested in the common stock of any one corporation at the time of purchase, and no more than 7% in any one corporation at fair market value. Furthermore, no more than 5% of the outstanding shares of any one company may be held. No more than the lesser of two times the sector weight in the index and 40% valued at market may be held in any one economic sector as defined by Morgan Stanley Capital International, Inc. Exposure to emerging markets securities shall be limited to 10% of the market value of the portfolio.

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

NOTE 3 - DEPOSITS AND INVESTMENTS: (continued)

The following table provides information as of September 30, 2007, concerning the fair value of investments, interest rate risk, and foreign currency risk:

TYPE OF INVESTMENT	INVESTMENTS				TOTAL VALUE	COST
	INVESTMENT MATURITIES AT FAIR VALUE (IN YEARS)					
	LESS THAN 1	1 - 5	6 - 10	MORE THAN 10		
<i>Fixed Maturity</i>						
Domestic:						
U.S. Government guaranteed		\$ 6,026,068	\$ 888,737	\$ 5,459,373	\$ 12,374,178	\$ 12,043,224
U.S. Agency Securities		11,584,006	2,335,858	5,430,702	19,350,566	19,373,048
Mortgage backed securities		3,581,807	1,085,541	80,368,764	85,036,112	84,718,002
Corporate bonds	\$ 2,276,030	9,101,200	10,693,139	7,793,123	29,863,492	30,262,985
Derivative instruments:						
TBA mortgage backed securities			101,313	35,174,268	35,275,581	35,296,284
Other derivative instruments	(286,035)				(286,035)	(196,534)
Total domestic fixed maturity	1,989,995	30,293,081	15,104,588	134,226,230	181,613,894	181,497,009
International:						
Australia				554,293	554,293	560,978
Bermuda			25,938		25,938	25,000
Brazil				200,625	200,625	180,900
Canada		63,800	126,066	379,003	568,869	579,651
Cayman Islands			6,503,430	3,550,970	10,054,400	11,571,854
Columbia				110,000	110,000	99,062
France			87,550		87,550	87,563
Germany			564,581	579,412	1,143,993	1,113,611
Iceland		1,001,968	295,105		1,297,073	1,288,948
India				130,914	130,914	139,681
Japan	32,776				32,776	
Luxembourg		144,789	1,509,776	419,497	2,074,062	2,112,813
Mexico			25,922	351,263	377,185	355,902
Netherlands		225,881	398,154	734,119	1,358,154	1,461,170
Panama				67,815	67,815	65,581
Russia			216,522	14,413	230,935	244,325
Singapore				140,391	140,391	149,482
United Kingdom				200,000	200,000	200,000
Total international fixed maturity	32,776	1,436,438	9,753,044	7,432,715	18,654,973	20,236,521
Total fixed maturity	2,022,771	31,729,519	24,857,632	141,658,945	200,268,867	201,733,530

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NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

NOTE 3 - DEPOSITS AND INVESTMENTS: (continued)

	TOTAL VALUE	COST
<i>Equities</i>		
Domestic	\$ 405,215,434	\$ 336,085,131
International:		
Australia - Australian Dollar	11,350,119	8,739,896
Austria - Euro	843,345	829,586
Belgium - Euro	5,449,863	4,909,487
Canada - Canadian Dollar	925,302	887,022
China - U.S. Dollar	1,395,421	1,128,124
Denmark - Krone	150,600	108,543
Finland - Euro	4,137,738	2,999,663
France - Euro	18,859,575	14,823,947
Germany - Euro	18,056,000	13,780,159
Greece - Euro	1,028,786	603,877
Hong Kong - Hong Kong Dollar	6,558,793	4,229,528
India - U.S. Dollar	503,256	537,469
Israel - Shekel	149,966	146,549
Italy - Euro	2,481,158	1,735,760
Japan - Yen	33,587,703	32,957,335
Luxembourg - Euro	1,681,111	884,508
Mexico - Neuvo Peso	631,757	651,592
Netherlands - Euro	8,906,518	6,956,808
New Zealand - New Zealand Dollar	73,362	72,863
Norway - Krone	644,732	619,490
Pakistan - Rupee	251,110	243,063
Russia - New Ruble	4,742,722	4,575,795
Singapore - Singaporean Dollars	2,841,246	1,741,755
Spain - Euro	2,950,815	2,618,677
Sweden - Krona	6,082,891	6,145,256
Switzerland - Franc	10,709,607	8,465,838
Taiwan - U.S. Dollar	888,906	947,155
Thailand - Baht	782,632	360,145
United Kingdom - Pound Sterling	32,533,787	27,478,190
Total international equities	179,198,821	150,178,080
Total equities	584,414,255	486,263,211
Total investments	\$ 784,683,122	\$ 687,996,741

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NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2007

NOTE 3 - DEPOSITS AND INVESTMENTS: (continued)

The following table provides information as of September 30, 2007, concerning credit risk:

RATING OF FIXED MATURITY INVESTMENTS			
Moody's Ratings§ (Unless Noted)	Fair Value	Cost	Fair Value as a Percent of Total Fixed Maturity Fair Value
Aaa	\$149,811,973	\$149,288,589	74.805%
AAA (SP)	4,349,690	4,340,543	2.172%
Aa1	664,491	663,446	0.332%
Aa2	91,765	100,179	0.046%
Aa3	3,247,493	3,257,686	1.622%
A1	3,543,303	3,545,092	1.769%
A2	515,841	516,206	0.258%
A3	1,444,505	1,471,504	0.721%
A- (SP)	171,488	174,971	0.086%
Baa1	6,073,681	6,414,030	3.033%
Baa2	7,357,093	8,280,934	3.674%
Baa3	7,318,025	7,878,549	3.654%
Ba1	4,701,300	4,769,719	2.347%
Ba2	1,566,149	1,577,253	0.782%
Ba3	1,689,453	1,657,660	0.844%
BB- (SP)	36,750	38,150	0.018%
B1	2,910,938	2,954,075	1.454%
B2	1,274,015	1,283,751	0.636%
B3	197,850	198,075	0.099%
Caa1	1,282,500	1,349,010	0.640%
Caa2	260,075	291,132	0.130%
Not rated	1,760,489	1,682,976	0.878%
	<u>\$200,268,867</u>	<u>\$201,733,530</u>	<u>100.000%</u>

§ - Moody's ratings are used when available. Standard & Poor's rating is used when it is available and a Moody rating is not available. Standard & Poor's ratings are denoted by (SP). Securities not rated primarily consist of commitments to purchase futures contracts and forward contracts.

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

NOTE 3 - DEPOSITS AND INVESTMENTS: (continued)

Securities lending program - The PACT Program's investment policy approved by the Board of Trustees permits the Program to enter into securities lending transactions defined as loans of securities to broker-dealers and other entities for collateral with a simultaneous agreement to return the collateral for the same securities in the future. There are no restrictions on the amount of loans that can be made. The PACT Program's custodian, Bank of New York, administers the program and acts as an agent for the PACT Program. Certain securities of the PACT Program are loaned to borrowers approved by the PACT Program. Approved borrowers of securities provide acceptable cash collateral in the form of federal funds or New York Clearing House funds as applicable for a particular loan. The Bank of New York has provided loss indemnification to the Program in the event that the borrower does not return the market value of the securities loaned. All security loans are open loans and can be terminated on demand by the PACT Program or the borrower. The initial collateral received shall have (i) in the case of loaned securities denominated in United States Dollars, cash collateral in the amount of 102% of the market value of the loaned securities or (ii) in the case of loaned securities which are not denominated in United States Dollars, cash collateral in the amount of 105% of the market value of the loaned securities. Pursuant to the terms of the applicable securities loan agreement, Bank of New York shall, in accordance with Bank of New York's reasonable and customary practices, mark loaned securities and collateral to their fair value each business day based upon the fair value of the collateral and the loaned securities at the close of the business employing the most recently available pricing information and receive and deliver collateral in order to maintain the value of the collateral at no less than 100% of the fair value of the loaned securities.

As of September 30, 2007, the average term of the loans was 37 days. Cash collateral investments are matured as needed to fulfill loan obligations. There is no direct matching of the maturities of the loans with the investments made with cash collateral.

The following describes the manner in which the Bank of New York is authorized to invest and reinvest cash collateral.

- Securities issued or fully insured by the United States government and any agency, instrumentality or establishments of the United States government (Government Securities).
- High-grade commercial paper, notes, bonds and other debt obligations including promissory notes, funding agreements and guaranteed investment contracts whether or not registered under the Securities Act of 1933, as amended. Such obligations may have fixed, floating, or variable rate interest payment provisions. Obligations maturing within one year shall be issued by issuers rated at least A-1 (by Standard & Poor's) or P-1 (by Moody's). Obligations maturing beyond one year shall be issued by issuers rated at least A (by Standard & Poor's) or A2 (by Moody's).
- Asset-backed securities which carry the highest credit rating by Standard & Poor's or Moody's.

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

NOTE 3 - DEPOSIT AND INVESTMENTS: (continued)

- Certificate of deposit, time deposits and other bank obligations of U.S. banks, their branches and subsidiaries. Obligations will be rated A-1 (Standard & Poor's) or P-1 (Moody's) if maturing within one year or rated A (Standard & Poor's) or A2 (Moody's) if maturing beyond one year.
- Repurchase and reverse repurchase agreements collateralized by approved investments.
- Securities, units, shares and other participations in money market funds, unregistered short-term investment funds, pools or trusts.
- Government securities having no maturity limit. Fixed rate instruments shall have a maturity of no greater than 13 months. Floating rate instruments rated "A" or "AA" shall have maturities no greater than three years with resets no less frequent than three months. Floating rate instruments rated "AAA" shall have maturities no greater than five years with resets no less frequent than three months.

At September 30, 2007, the fair value of the securities on loan was \$68,771,726. The fair value of the cash collateral pledged by the borrowers was \$71,259,169. The PACT Program has no credit risk exposure to borrowers because the amounts the Program owes the borrowers exceeds the amounts the borrowers owe the Program. There were no significant violations of legal or contractual provisions, no borrower or lending agent default losses, and no recoveries of prior period losses during the year.

Investments purchased with cash collateral are held by the custodial agent, but not in the name of the PACT Program. The following table provides information as of September 30, 2007 concerning securities lent:

SECURITIES LENDING - INVESTMENTS LENT AND COLLATERAL RECEIVED

(at Fair Value)

	FAIR VALUE OF UNDERLYING SECURITIES	CASH COLLATERAL INVESTMENT VALUE
<u>Securities Lent</u>		
<i>For cash collateral</i>		
Domestic Fixed Maturities	\$ 7,778,726	\$ 7,964,054
Domestic Equity	60,993,000	63,295,115
Total securities lent	<u>\$ 68,771,726</u>	<u>\$ 71,259,169</u>

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

NOTE 3 - DEPOSIT AND INVESTMENTS: (continued)

Mortgage-backed securities - As of September 30, 2007, the PACT Program had investments in mortgage-backed securities. Embedded prepayment options cause these investments to be highly sensitive to changes in interest rates. Prepayments by the obligees of the underlying assets reduce the total interest payments to be received. Generally, when interest rates fall, obligees tend to prepay the mortgages thus eliminating the stream of interest payments that would have been received under the original amortization schedule. The resulting reduction in cash flow diminishes the fair value of mortgage-backed securities. Maturities may differ from contractual maturities (as shown in the table of investments) in mortgage-backed securities due to prepayment characteristics of these securities. Average life is an acceptable expected maturity.

At September 30, 2007, the PACT Program had investments in forward settling TBA mortgage-backed securities in the amount of \$35,296,285. Included in other liabilities on the Statement of Fiduciary Net Assets is a corresponding liability for the same amount. Generally, these securities are closed with a gain or loss prior to settlement. However, the PACT Program would be obligated for these amounts should the securities be delivered.

NOTE 4 - FUTURE TUITION BENEFIT PAYMENTS AND FUTURE CONTRACT PAYMENTS:

An actuary determines future tuition benefit payments and future contract payments. The standardized measurement is the actuarial present value of such payments. This valuation method reflects the present value of estimated tuition benefits that will be paid in future years and the present value of estimated contract payments that will be received from installment contract purchasers in future years. The significant actuarial assumptions used and results from the most recent valuation are as follows:

Date of latest actuarial valuation	September 30, 2007
------------------------------------	--------------------

Assumptions:

Rate of return on investments	8.07% for the period 2007 - 2008 to 2011 - 2012; 8.50% thereafter
Future tuition increases	7.25%
Enrollment of beneficiaries	10% will attend a junior/community college first five years; 11% tuition bias for four-year universities; 3% tuition bias for two-year colleges

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

NOTE 4 - FUTURE TUITION BENEFIT PAYMENTS AND FUTURE CONTRACT PAYMENTS: (continued)

Assumptions: (continued)

Contract cancellations

The actuarial valuation recognizes cancellations in accordance with the following schedule:

	<u>LUMP SUM</u>	<u>60 MONTHLY PAYMENTS</u>	<u>EXTENDED MONTHLY PAYMENTS</u>
Year of purchase	0.5%	5%	6%
Year of purchase +1	0.5%	2%	5%
Year of purchase +2	0.5%	1%	4%
Year of purchase +3	0.5%	1%	4%
Year of purchase +4	0.5%	1%	3%
Thereafter	0.5%	1%	2%

The assumptions shown above do not reflect the initial involuntary cancellations that result shortly after each enrollment period for contract purchasers who never make payments on their contracts.

Payment of tuition and
mandatory fees

128 credit hours utilization

<u>SEMESTER</u>	<u>ASSUMPTIONS</u>
Fall	45% of payments, November 1
Spring	45% of payments, March 1
Summer	10% of payments, August 1

Results:

Actuarial present value of future payments expected to be made
for tuition, fees and contract cancellations for all contracts sold \$836,909,570

Actuarial present value of future payments expected to be
received from installment contract purchasers 53,309,201

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

NOTE 4 - FUTURE TUITION BENEFIT PAYMENTS AND FUTURE CONTRACT PAYMENTS: (continued)

The significant actuarial assumptions used for the actuarial valuations for September 30, 2006 and 2005 are as follows:

Assumptions:

Rate of return on investments	7.92% for the period 2006 - 2007 to 2010 - 2011 and 8.5% thereafter for 2006; 7.88% for the period 2005 - 2006 to 2009 - 2010 and 8.5% thereafter for 2005
Future tuition increases	7.25% for 2006 and 2005
Enrollment of beneficiaries	17.5% will attend a junior/community college for first two years for 2006 and 2005; 8% tuition bias for four-year universities for 2006 and 5% for 2005; 3% tuition bias for two-year colleges for 2006 and 0% for 2005
Contract cancellations	The actuarial valuation recognizes cancellations in accordance with the following schedule for 2006 and 2005:

	<u>Lump Sum</u>	<u>60 Months</u>	<u>Extended</u>
Year of purchase	0.5%	5%	6%
Year of purchase +1	0.5%	2%	5%
Year of purchase +2	0.5%	1%	4%
Year of purchase +3	0.5%	1%	4%
Year of purchase +4	0.5%	1%	3%
Thereafter	0.5%	1%	2%

Payment of tuition and mandatory fees

128 credit hours utilization

For 2006 and 2005:

<u>Semester</u>	<u>Assumptions</u>
Fall	45% of payments, November 1
Spring	45% of payments, March 1
Summer	10% of payments, August 1

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2007

REQUIRED SUPPLEMENTARY INFORMATION

Schedule of Funding Progress for the PACT Program is as follows:

	NET ASSETS AVAILABLE FOR BENEFITS	ACTUARIAL VALUE OF FUTURE CONTRACT PAYMENTS	TOTAL ASSETS	ACTUARIAL PRESENT VALUE OF FUTURE TUITION BENEFIT PAYMENTS	ASSETS IN EXCESS (DEFICIT) OF TUITION BENEFIT PAYMENTS	ASSETS AS A PERCENTAGE OF TUITION BENEFIT PAYMENTS
September 30, 2006 (as restated)	\$691,595,188	\$54,404,134	\$745,999,322	\$806,535,334	(\$60,536,012)	92.5%
September 30, 2007	763,858,689	53,309,201	817,167,890	836,909,570	(19,741,680)	97.6%

NOTE 5 - TAX STATUS:

The Internal Revenue Code provides that state tuition plans that meet certain requirements are exempt from income taxation. The PACT Program's rules and regulations meet those requirements. Accordingly, no provision for income taxes has been made in these financial statements for accrual of income taxes for the year ended September 30, 2007, nor for prior years.

NOTE 6 - PRIOR PERIOD ADJUSTMENT

The beginning net assets as of October 1, 2006 have been restated by \$22,660,802 to reflect the Fall 2006 tuition benefits obligation as a liability at September 30, 2006. The Fall 2006 tuition benefits obligation was previously included in the Actuarial Present Value of Future Benefit Payments. The Actuarial Present Value of Future Benefit Payments was also restated by the same amount as shown in the Schedule of Funding Progress (see note 4). The impact of the reclassification on the PACT Program's Schedule of Funding Progress was a decrease of 0.2% in the Assets as a Percentage of Tuition Benefit Payments.

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM
MONTGOMERY, ALABAMA

COMBINING STATEMENT OF FIDUCIARY NET ASSETS
SEPTEMBER 30, 2007

	TRUST FUND	ADMINISTRATIVE FUND	TOTAL
ASSETS:			
Cash and cash equivalents	\$ 38,145,410	\$ 390,544	\$ 38,535,954
Accounts receivable	1,311,259		1,311,259
Interest receivable	2,382,986		2,382,986
Foreign taxes receivable	375,799		375,799
Investments	784,683,122		784,683,122
Invested securities lending collateral	71,259,169		71,259,169
Total assets	<u>898,157,745</u>	<u>390,544</u>	<u>898,548,289</u>
LIABILITIES:			
Amounts due to State			
Treasury	36,129		36,129
Due to (from) other fund	26,808	(26,808)	
Warrants and accounts payable	27,859,963	162,720	28,022,683
Accrued liabilities		75,334	75,334
Other liabilities	35,296,285		35,296,285
Securities lending collateral	71,259,169		71,259,169
Total liabilities	<u>134,478,354</u>	<u>211,246</u>	<u>134,689,600</u>
NET ASSETS:			
Held in trust for tuition payments and other purposes	<u>\$ 763,679,391</u>	<u>\$ 179,298</u>	<u>\$ 763,858,689</u>

See Independent Auditors' Report on supplementary information.

ALABAMA PREPAID AFFORDABLE COLLEGE TUITION PROGRAM

COMBINING STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
FOR THE YEAR ENDED SEPTEMBER 30, 2007

	TRUST FUND	ADMINISTRATIVE FUND	TOTAL
ADDITIONS:			
Contract payments	\$ 28,865,379		\$ 28,865,379
Investment income:			
From investing activities:			
Interest and dividend income	22,545,340		22,545,340
Gain on investments	83,073,338		83,073,338
Net investment income from investing activities	105,618,678		105,618,678
From securities lending:			
Securities lending income	1,167,482		1,167,482
Less: securities lending expenses			
Borrower rebates	1,091,314		1,091,314
Management fees	22,736		22,736
Total securities lending expenses	1,114,050		1,114,050
Net income from securities lending activities	53,432		53,432
Total investment income	105,672,110		105,672,110
Other income	201,506	\$ 662,844	864,350
Total additions	134,738,995	662,844	135,401,839
DEDUCTIONS:			
Benefits	54,885,211		54,885,211
Salaries and other			
administrative expenses		345,389	345,389
Professional services	2,940,821	985,398	3,926,219
Cancellation refunds	3,981,519		3,981,519
Total deductions	61,807,551	1,330,787	63,138,338
CHANGES IN NET ASSETS BEFORE TRANSFERS	72,931,444	(667,943)	72,263,501
TRANSFERS TO (FROM)	(600,000)	600,000	
CHANGES IN NET ASSETS	72,331,444	(67,943)	72,263,501
NET ASSETS AT BEGINNING OF YEAR AS ORIGINALLY STATED	714,008,749	247,241	714,255,990
PRIOR PERIOD ADJUSTMENT	(22,660,802)		(22,660,802)
NET ASSETS AS RESTATED	691,347,947	247,241	691,595,188
NET ASSETS AT END OF YEAR	\$ 763,679,391	\$ 179,298	\$ 763,858,689

See Independent Auditors' Report on supplementary information.